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No. 561

In the

Supreme Court of the United States

OCTOBER TERM, 1958

UNITED STATES OF AMERICA,

Petitioner,

v.

HINE PONTIAC,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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OPINION BELOW

The opinion of the United States District Court in UNITED STATES v. HINE PONTIAC is not officially reported, but is unofficially reported in C. C. H. Paragraph 9210 and 1 A. F. T. F. 2d 58-734.

JURISDICTION

Jurisdiction is sought under provisions of 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

Whether the amounts which certain finance companies credited to a dealer's reserve account in taxpayer's name should be taken into taxpayer's income when so credited where taxpayer was on an accrual basis of accounting; and in the alternative, whether or not the amount retained in such reserve account constitutes a reasonable reserve for bad debts. (See Stipulation filed in the United States Court of Appeals for the Fifth Circuit, Appendix A.)

STATEMENT OF CASE

This is a suit by Hine Pontiac, a corporation, to recover taxes paid upon a deficiency assessed against it for alleged income arising out of dealer's reserves during the taxable years 1953 and 1954. In connection with the operation of its business, Hine Pontiac sold both new and used automobiles on time payment or installment plan of purchase. After the purchase price of the automobile has been agreed upon by Hine Pontiac and the purchaser, the sale is not concluded *unless* and *until* a finance company agrees to accept the note of the purchaser for the balance of the purchase price plus finance charges (Stipulation 13 R. 26). Certain portions of the finance charges are set up in a special account called "dealer's reserve account." This credit to Hine Pontiac by the finance company on the "dealer's reserve account" is made immediately upon the assignment of the note even though the proceeds from said notes have not been collected and will not be collected for

an average period of two years and until the purchaser of the automobile pays the note in full (Stipulation 13 R. 26-27). Hine Pontiac is not entitled to any payments or to use any funds from this account except to the extent that it exceeds a stated percentage of the unpaid balances of notes acquired from Hine Pontiac on the settlement dates called for by the respective contracts. Thus the finance company admits no liability to Hine Pontiac until the "dealer's reserve account" reaches a specified relation to the unpaid balance of notes acquired from Hine Pontiac and then only with respect to the amount by which the "dealer's reserve account" exceeds this minimum on the agreed settlement dates (Stipulation 13 R. 27). The deficiency, therefore, was assessed against the "dealer's reserve account" to which the finance company admitted no liability to Hine Pontiac until termination of the contract with the finance company and full payment of the notes by the makers thereof (Stipulation 13 R. 27). The finance company thus used the "dealer's reserve account" as a contingency fund to absorb its losses on the notes acquired from Hine Pontiac on a nonrecourse basis (Stipulation 13 R. 28). Also, the reserve was subject to being decreased by prepayment of notes of customers prior to the time they were due (Stipulation 13 R. 28).

Hine Pontiac plead and proved that it kept its books on the accrual basis of accounting and also used the reserve method of accounting for bad debts (Stipulation 4 R. 24). It further plead in the alternative that the amounts set up in the "dealer's reserve account" constituted a reasonable

and proper reserve for bad debts (R. 13 and 14). By stipulation it showed that on December 31, 1953, the total outstanding balance of notes was Eight Hundred Sixty-Six Thousand Eight Hundred Sixty-Four Dollars and Sixty-Nine Cents ($866,864.69) and as of December 31, 1954, it had a total outstanding balance of notes of Two Million Four Hundred Twelve Thousand Nine Hundred Nine Dollars and Four Cents ($2,412,909.04). (Stipulation 23 R 30.) It also showed by stipulation that its experience on losses sustained through dealer's reserves was four and nine-tenths per cent (4.9%) in 1953, and three and two hundred thirty-two thousandths per cent (3.232%) in 1954 of the amount of losses as compared to the amount of notes outstanding (Stipulation 24 R. 30).

Also, testimony was introduced to show that four per cent (4%) constituted a reasonable reserve for bad debts (R. 73-74). By simple computation and multiplication of such loss ratio times the amount of notes outstanding it is demonstrated that the amount of reserves held by the finance companies constituted an amount less than the amount of a reasonable reserve for bad debts for Hine Pontiac, so that in any event the amount set up by the finance companies in the "dealer's reserve account" would constitute a reasonable reserve for bad debts for Hine Pontiac. It was also proved that the finance companies themselves do not treat as income any amount placed to an unearned discount account which is what the "dealer's reserve account" is (R. 72-73).

Hine Pontiac paid the deficiencies of Sixteen Thousand Twenty-Seven Dollars and Fifty-Four Cents ($16,027.54) and Twenty-Six Thousand Three Hundred Eighty-One Dollars and Forty-Seven Cents ($26,381.47) for 1953 and 1954 plus interest of Five Thousand Five Hundred Eighty-One Dollars and Ninety-One Cents ($5,581.91), and then filed claims for refund which were denied and the United States District Court entered judgment for Hine Pontiac in the amount of Forty-Two Thousand Four Hundred Nine Dollars and One Cent ($42,409.01) plus assessed interest in the amount of Five Thousand Five Hundred Eighty-One Dollars and Ninety-One Cents ($5,581.91), or the total sum of Forty-Seven Thousand Nine Hundred Ninety Dollars and Ninety-Two Cents ($47,990.92), together with interest, and the United States District Court in holding in favor of Hine Pontiac said:

> "It is the soul and life blood of a tax against the citizen, that the citizen should have received something which justifies the tax."

By stipulation (Appendix A) the Court of Appeals affirmed the United States District Court.

REASONS FOR DENYING THE WRIT

The question in this case is not the same as that presented in COMMISSIONER v. JOHN HANSEN AND SHIRLEY G. HANSEN, NO. 380, THIS TERM, and in COMMISSIONER v. BURL P. GLOVER, NO 381, THIS TERM. The facts are different and neither case contained the issue that the "dealer's reserve account" constituted a reasonable reserve for bad debts.

Furthermore, it is certainly beyond the realm of reason to state that the amount held by the finance company in the "dealer's reserve account" constitutes a right of the taxpayer to receive the same (SPRING CITY FOUNDRY COMPANY v. COMMISSIONER, 292 U. S. 182), when the amount so to be assessed against the taxpayer is subject to the following contingencies and uncertainties:

> (a) The credits to the "dealer's reserve account" are made before any payments have been collected or notes paid to said account, and may never be collected if the purchaser does not pay the same.
>
> (b) Losses of the finance company are chargeable against the account.
>
> (c) Hine Pontiac, the dealer, has no control over the account, and the account remains wholly in the control of the finance company.
>
> (d) Notes which are prepaid by purchasers reduce the "dealer's reserve account."

It should always be remembered and borne in mind as stipulated by the parties that this is one transaction and the car is not sold until the finance company approves the credit of the purchaser. Thus it is one simultaneous transaction and does not constitute a separate transaction of the car being sold to the purchaser and the note being sold to the finance company. These facts are different and when coupled with the proposition involved herein for a reasonable reserve for bad debts constitutes ample reason why the writ of certiorari should be denied and the same

should not be held in abeyance pending the decision in the *Hansen* and *Glover* cases.

Respectfully submitted,

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Attorney of Record for Respondent.

L. W. ANDERSON,
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By .....

CERTIFICATE OF SERVICE

Respondent, Hine Pontiac, served three copies of Respondent's Brief in Opposition, in accordance with Rule 33, Subsections 1 and 3(b), by depositing copies of the Brief in the United States Post Office at Dallas, Texas, Air Mail, postage-prepaid, addressed to Counsel of Record for Petitioner, J. Lee Rankin, Solicitor General, Department of Justice, Washington 25, D. C.

.....

PAUL J. SEDGWICK,
Barr Building,
910 Seventeenth Street, N. W.,
Washington, D. C.,
Attorney of Record for Respondent.

APPENDIX "A"

STIPULATION OF THE PARTIES FILED:
September 6, 1958

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NO. 17,242

UNITED STATES OF AMERICA,
APPELLANT

V.

HINE PONTIAC,
APPELLEE

ON PETITION FOR REVIEW OF THE DECISION OF
THE UNITED STATES DISTRICT COURT FOR
THE NORTHERN DISTRICT OF TEXAS

STIPULATION

The parties to the above-entitled proceedings, by their counsel of record, hereby stipulate as follows:

1. Whereas one of the issues in this case is whether certain amounts which several finance companies credited to a reserve account in taxpayer's name should be taken into taxpayer's income when so credited where taxpayer was on an accrual basis of accounting; and in the alternative, whether or not the amount retained in such reserve account constitutes a reasonable reserve for bad debts;

2. Whereas in certain respects the first issue was decided by this Court on January 7, 1958, in *Texas Trailercoach, Inc.* v. *Commissioner*, 251 F. 2d 395, and on February 6, 1958, in *West Pontiac, Inc.* v. *Commissioner*, both in favor of the taxpayer;

3. Whereas the parties to this proceeding desire to avoid further expense in connection with the appeal; and the appellant is willing, without conceding the correctness of the appellee's position, that the case be disposed of without briefing and oral argument;

NOW THEREFORE, it is stipulated and agreed by and between the parties, by their counsel of record, that, subject to the approval of the Court, the case may be disposed of without briefing and argument in accordance with the proposed order attached.

/s/ CHARLES K. RICE

CHARLES K. RICE
Attorney for Appellant

/s/ L. W. ANDERSON

L. W. ANDERSON
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Dallas 1, Texas
Attorney for Appellee

September 4, 1958

A true copy.
Test: EDWARD W. WADSWORTH
Clerk, U. S. Court of Appeals, Fifth Circuit

By /s/ Gilbert F. Ganushean
Deputy

New Orleans, Louisiana